

Message Text

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ACTION EUR-25

INFO OCT-01 EA-11 ADP-00 AID-20 CEA-02 CIAE-00 COME-00

EB-11 FRB-02 INR-09 IO-12 NEA-10 NSAE-00 RSC-01

OPIC-12 TRSE-00 CIEP-02 LAB-06 SIL-01 SAL-01 OMB-01

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E. O. 11652: N/ A

TAGS: EFIN, OECD

SUBJECT: JAPANESE INVOCATION OF AN ARTICLE 7(B) DEROGATION TO
CAPITAL CODE

REF: (A) OECD 05204

(B) DAF/ INV/ 73/5

(C) DAF/ INV/73/1 AND ADDENDUM

PASS TREASURY FOR KORP

1. SUMMARY. AS RESULT OF MEASURES TAKEN OCTOBER 20, 1972,
JAPAN HAS INFORMED ORGANIZATION OF ITS INTENTION TO INVOKE
ARTICLE 7(B) OF CAPITAL MOVEMENTS CODE (CMC). REQUESTED
DEROGATION WILL COVER NEW JAPANESE RESTRICTIONS ON
PURCHASE BY NON- RESIDENTS IN JAPAN OF SECURITIES (ITEMS
IV/ A1 AND 3 IN CMC). JAPANESE JUSTIFY DEROGATION ON
GROUNDS THAT AN EXCESSIVE INFLOW OF FOREIGN CAPITAL BEGIN-
NING SEPTEMBER 1972 CAUSED " SERIOUS ECONOMIC AND FINANCIAL
DISTURBANCE." THIS CABLE AMPLIFIES OUR REPORT IN REF (A).
ACTION REQUESTED. DEPT. RESPONSE TO PARA 4 BELOW. END
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SUMMARY.

2. DISCUSSION OF MAJOR PROBLEM: IN ITS MEETING FEB. 19-20 (REF A) INVISIBLES COMMITTEE FOUND IT DIFFICULT TO JUSTIFY JAPANESE DEROGATION. AS POINTED OUT BY SECRETARIAT IN REF (B), NET INFLOW OF CAPITAL (BALANCE OF PAYMENTS BASIS) THROUGH SECURITY TRANSACTIONS IN SECOND AND THIRD QUARTERS 1972 AMOUNTED TO ONLY US\$71 MILLION. FURTHERMORE, TOTAL NET CAPITAL INFLOW OF US\$400 MILLION BETWEEN APRIL AND SEPTEMBER 1972 WAS ONLY EQUIVALENT TO 5.2 PERCENT OF THE INCREASE IN MONEY SUPPLY (NARROWLY DEFINED M1) AND TO 2 PERCENT OF INCREASE OF COMMERCIAL BANK LOANS AND DISCOUNTS. JAPANESE EXPERTS ARGUED THAT NET FOREIGN PURCHASES OF JAPANESE SECURITIES HAD CONTRIBUTED TO SHARP INCREASE OF SECURITY PRICES ON TOKYO STOCK EXCHANGE, AND HAD THUS CREATED SERIOUS DISTURBANCE. U. S. EXPERT QUESTIONED THE IMPLIED CAUSAL RELATIONSHIP. IT MIGHT JUST AS WELL BE THE REVERSE - EG, THAT STEEP RISE IN JAPANESE SECURITIES PRICES MAINLY DUE TO DOMESTIC FLOWS HAD ATTRACTED FOREIGN FUNDS. HE ALSO BELIEVED THAT AMOUNT OF FOREIGN FUNDS THOUGHT TO HAVE MOVED INTO JAPANESE SECURITY MARKET WAS TOO SMALL TO BE CONSIDERED MAJOR DISTURBANCE EITHER TO THAT MARKET OR TO JAPANESE ECONOMY. JAPANESE EXPERTS ARGUED THAT NET PURCHASE OF SECURITIES WAS ADMITTEDLY ONLY ONE OF SEVERAL FACTORS CONTRIBUTING TO NET INCREASE OF JAPANESE OFFICIAL RESERVES, BUT THAT IT MIGHT HAVE PLAYED MORE SIGNIFICANT ROLE IF AUTHORITIES HAD NOT MOVED IN OCTOBER TO RESTRICT SUCH PURCHASES. U. S. EXPERT POINTED OUT THAT INCREASE IN OFFICIAL RESERVES NOT ACCEPTABLE RATIONALE FOR 7(B) DEROGATION. COMMITTEE RAISED GENERAL QUESTION WHETHER SERIOUS DISTURBANCE IN ONLY ONE SECTOR OF JAPANESE ECONOMY COULD JUSTIFY AN ARTICLE 7(B) DEROGATION. IT ASKED SECRETARIAT TO TAKE NOTE OF THIS QUESTION IN PREPARING COMMITTEE' S DRAFT REPORT TO COUNCIL ON JAPANESE DEROGATION, WHICH WILL BE DISCUSSED AT THE COMMITTEE' S NEXT MEETING IN APRIL.

3. OTHER POINTS: COMMITTEE NOTED THAT JAPANESE RESTRICTIONS ON CAPITAL INFLOW THROUGH SECURITIES MARKET WERE ACCOMPANIED BY MEASURES TO REMOVE RESTRICTIONS ON CAPITAL OUTFLOW THROUGH PURCHASE BY RESIDENTS OF FOREIGN MUTUAL FUNDS. THIS WILL PERMIT JAPAN TO AMEND ITS RESERVATIONS TO LIMITED OFFICIAL USE

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SEVERAL CODE ITEMS. COMMITTEE ALSO NOTED THAT JAPANESE

AUTHORITIES HAVE INTRODUCED MEASURES TO MAKE CHARTER CONTRACTS CONCERNING SHIPS AND AIRPLANES EXPORTED FROM JAPAN AFTER OCTOBER 23, 1972, SUBJECT TO VERIFICATION BY BANK OF JAPAN (PP 8-9, REF C). SECRETARIAT NOTED THAT THIS MEASURE, ALTHOUGH APPARENTLY OF NO REAL EFFECT, REQUIRES JAPAN TO LODGE AN ARTICLE 7(B) DEROGATION AGAINST ITEMS C/ 1 AND C/4 (MARITIME FREIGHTS AND AIR TRANSPORT, INCLUDING CHARTERING) IN INVISIBLES CODE.

4. ACTION REQUESTED: DESPITE INITIAL DISFAVOR WITH JAPANESE JUSTIFICATION FOR THIS DEROGATION, IT SEEMS UNLIKELY THAT MAJORITY OF INVISIBLES COMMITTEE COULD BE PERSUADED AT NEXT MEETING THAT JAPAN UMJUSTIFIED IN INVOCATION OF 7(B) DEROGATION. SINCE NO OTHER LEGAL BASIS POSSIBLE FOR SURPLUS COUNTRY UNDER CMC, ONLY ALTERNATIVE WOULD BE REMOVAL OF JAPANESE RESTRICTIONS AND CANCELLATION OF DEROGATION REQUEST. THIS SEEMS UNLIKELY PROSPECT UNLESS JAPAN CAN BE CONVINCED TO DO THROUGH BILATERAL NEGOTIATIONS. DEPARTMENT AND EMBASSY TOKYO MAY WISH TO COMMENT AS TO WHETHER THEY BELIEVE JAPANESE RESTRICTIONS ON PURCHASE BY NON- RESIDENTS OF DOMESTIC SECURITIES ARE IN FACT SERVING JUSTIFIABLE ROLE ON THWARTING " SERIOUS ECONOMIC DISTURBANCE." IF DEPT. BELIEVES THAT JAPANESE RESTRICTIONS ARE NOT JUSTIFIABLE UNDER CMC, THEN WE WOULD APPRECIATE INSTRUCTIONS AS TO HOW TO HANDLE THIS MATTER WHEN INVISIBLES COMMITTEE' S FINAL REPORT TO COUNCIL GOES TO PAYMENTS COMMITTEE.

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